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TAGS: ECON EPET PGOV EINV EC
SUBJECT: CONSTITUENT ASSEMBLY ELIMINATES PETROLEUM FUNDS, GRANTS EXPANDED BUDGET POWER TO MINISTRY OF FINANCE

REF: Quito 55

¶1. (U) Summary: The Constituent Assembly approved a law, drafted by the Correa Administration, that closes the petroleum reserve funds and moves that financing on to the regular budget. It stipulates that those resources can only be used for investment, and establishes a broad budget requirement that current expenditures cannot be funded by borrowing or petroleum revenue. It also gives increased budgetary discretion to the Minister of Finance. End Summary.

¶2. (U) On April 2, the Constituent Assembly approved the "Law to Recover the Use of Petroleum Resources and Rationalize Debt Administrative procedures." This is the second law approved by the Constituent Assembly, following the tax reform law (reftel).

¶3. (U) The law has three broad objectives: bringing the petroleum funds on to the budget, increasing the Ministry of Finance's flexibility to take on new debt and increase the budget, and replacing the budget guidelines in the Fiscal Responsibility Law with a broader guideline.

Eliminating Petroleum Funds

¶4. (U) The law eliminates four "petroleum funds" and incorporates the funds' unallocated balances into the general budget. In March, the combined value of the funds was $1.93 billion. Revenues that previously had gone into reserve funds will now go directly into the general budget. Each of the funds had complex spending requirements, which have now been deleted, although the government has stated that it will continue to direct some of the revenues to the same purposes as before. The new law stipulates that these petroleum revenues must be used for investment and cannot be used for current expenditures.

New Broad Budget Guideline

¶5. (U) The new law also replaces the broad limits on government spending established in the Fiscal Responsibility Law. The old guideline had been that government spending, in real terms, could not increase by more than 3.5% of GDP per year. The new guideline is that current expenditures cannot be financed by debt or by income from petroleum exports.

The Debt Committee and Ministry Authority

¶6. (U) The new law also modifies the requirements for the government to take on debt and increase the budget, although the version approved by the Constituent Assembly gives the Minister of Finance less autonomy than had the version drafted by the administration.

¶7. (U) Previously the Central Bank had to give a favorable approval before the government could take on a new loan; with the new law, it loses that authority. The administration had proposed that the Ministry of Finance have sole responsibility in approving new debt, but the Assembly instead established a Debt and Financing Committee. The Committee consists of the President, the Minister of Economy and Finances and the Secretary of Planning. In addition, any minister requesting a credit will be allowed to speak before the Committee but will not have a vote. Only debts that exceed 0.15% of national budget will have to be approved by the Committee; lesser amounts can be approved by the Minister of Finance.

¶8. (U) The new law also allows the Ministry of Finance to increase or reduce the national budget by 15 percent without consulting Congress. (The Assembly limited the Ministry's discretion at 15%; the draft submitted by the administration would have given the Ministry unlimited discretion to increase the budget.) Previously the Ministry could modify the budget by up to five percent.

Analysts Comments in Favor and Against the Changes
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¶9. (SBU) Former Minister of Finance Magdalena Barreiro told the press the law will give the government greater flexibility to better manage its resources. Jaime Carrera, economic analyst at the Fiscal Policy Observatory, an NGO, believes that fiscal power concentrated in the hands of one party will undermine future decisions by Congress, and told the Embassy he feels the move replicates the

absence of controls on fiscal spending that existed during the 1970s petroleum boom.

COMMENT

¶10. (SBU) The new law appears to reduce the constraints on spending established by a series of laws, notably the Fiscal Responsibility Law, and those creating the petroleum funds. In reality, the law recognizes and simplifies a number of practices that were already in place. Current and previous administrations bent the intent of the petroleum funds by issuing emergency decrees, and readily violated the 3.5% growth gap on budget. However, previously governments had to go through some budgetary and legal gymnastics to get around the rules, and now they will not. It remains to be seen whether the new flexibility will allow the government to spend more wisely, as the government contends, or give the Ministry of Finance too much discretion, as some critics contend.

¶11. (SBU) The new law does establish some reasonable budgetary constraints: limiting petroleum revenues to investments and requiring that current expenses be funded by current revenues. However, we suspect that the government will work around these new guidelines if it feels the need, just as governments had violated the previous constraints.

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